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No. 753

IN THE

Supreme Court of the United States

OCTOBER TERM, 1962

WESTINGHOUSE BROADCASTING COMPANY, INC.,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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January 16, 1963

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1962

WESTINGHOUSE BROADCASTING COMPANY, INC., *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Westinghouse Broadcasting Company, Inc., (Broadcasting) prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit, entered in this action October 19, 1962.

Opinions Below

The opinion of the Tax Court (R. 104a-123a*) is reported at 36 T. C. 912. The opinion of the Court of Appeals affirming the decision of the Tax Court (App. 4a-11a**) is reported at 309 F. 2d 279.

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*"R." references are to Petitioner's Appendices in the Court of Appeals.

**"App." references are to the Appendix to this Petition.

Jurisdiction

The judgment of the Court of Appeals was entered October 19, 1962 (R.). The jurisdiction of this Court is invoked under 28 U. S. C. § 1254(1).

Question Presented

Is a business contract for a fixed term, with a provision for renewal terms if the parties mutually consent, rendered non-depreciable as a matter of law for Federal income tax purposes by reason of the fact that there is uncertainty whether the parties will consent to renewal?

The Court below answered that question in the affirmative and adopted as its rule of law that depreciation was not allowable because there was uncertainty as to the number of renewals. It held that in order to be allowed depreciation Broadcasting should have proved that there was reasonable certainty that the contract would not be renewed, either at the end of the current term or at the end of an identified future renewal term.

It is Broadcasting's contention that under the proper rule of law the contract was depreciable over its term in effect at the end of the taxable year because there was uncertainty as to renewal. It is only where it appears from the record that a renewal term or terms are reasonably certain to occur that such renewal terms are added to the depreciable life of the contract.

Under the rule of law contended for by Broadcasting, the uncertainty as to the exercise of the renewal provision renders the contract depreciable over its term in effect at the end of the taxable year; but under the rule of law adopted by the Court below, such uncertainty of renewal renders the contract non-depreciable.

The Court below stated that Broadcasting had failed to prove with reasonable certainty the number of renewal terms which would actually occur, but under the rule of law contended for by Broadcasting such proof was not required. The question presented to this Court thus does not involve burden of proof but rather what is the proper rule of law to be applied to the undisputed facts.

Statutes and Regulations Involved

The statutes and regulations involved are Section 23(l) of the Internal Revenue Code of 1939, 53 Stat. Part I 14, as amended by 56 Stat. 798,819; Section 167(a)(1) of the Internal Revenue Code of 1954, 68A Stat. 51-52; Regulations 118, Sections 39.23(a)-10(b) and 39.23(1)-3, 26 CFR (Revised 1953) Sections 39.23(a)-10(b) and 39.23(1)-3; and Income Tax Regulations, Sections 1.162-11(b)(2) and 1.167(a)-3, 26 CFR (Revised 1953) Sections 1.162-11(b)(2) and 1.167(a)-3. Said statutes and regulations are set forth in the Appendix hereto at pages 1a-3a.

Statement

This petition seeks review of a judgment determining deficiencies in Federal income tax of Broadcasting for the years 1953 and 1954 in the amounts of $363,371.93 and $622,410.13, respectively, and denying Broadcasting refunds of Federal income tax for those years.

Broadcasting commenced this proceeding on January 7, 1959, in the Tax Court of the United States (R. 1a). The basic facts in the case are not disputed, being in part stipulated by the parties and in part established by the uncontradicted testimony of an expert witness (R. 2a-103a, 125a). Those facts are:

On June 1, 1953, Broadcasting purchased from Philco Corporation (Philco) all the assets of the Philadelphia television station WPTZ for $8,534,924.94. Among such assets of WPTZ was a network affiliation agreement between National Broadcasting Company (NBC) and Philco for a two year term ending January 1, 1954. Of the aggregate purchase price, $5,000,000 was allocated to the network affiliation agreement (R. 3a-4a, 105a-106a).

On June 1, 1953, Broadcasting commenced operation of television station WPTZ as an NBC affiliate under the network affiliation agreement (R. 4a, 106a).

Federal Communications Commission (FCC) regulations in effect during 1953 and 1954 prohibited any contract providing for network affiliation for a term longer than two years. 47 CFR (Revised 1953) Sec. 3.658(c).* The network affiliation agreement contained the following provision:

> "23. This agreement . . . shall remain in effect for a period of two years. It shall then be renewed on the same terms and conditions for a further period of two years, and so on for successive further periods of two years each unless and until either party shall, at least three months prior to the expiration of the then current term, give the other party written notice that it does not desire to have the contract renewed for a further period." (R. 35a-36a)

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*"(c) *Term of affiliation.* No license shall be granted to a television broadcast station having any contract, arrangement, or understanding, express or implied, with a network organization which provides, by original terms, provisions for renewal, or otherwise for the affiliation of the station with the network organization for a period longer than 2 years: *Provided,* That a contract, arrangement, or understanding for a period up to 2 years may be entered into within 6 months prior to the commencement of such period." (47 CFR (Revised 1953) § 3.658(c).)

Neither Broadcasting nor NBC gave notice of non-renewal pursuant to the above-mentioned provision of the network affiliation agreement on or prior to October 1, 1953, and on that date the affiliation agreement between NBC and WPTZ was therefore renewed for a two-year term expiring January 1, 1956 (R. 13a).

Television networks found it advantageous to own the maximum number of VHF television stations (five) permitted by regulations of the FCC, 47 CFR (Revised 1953) § 3.636(a)(2), and to own such stations in the largest markets. In 1953 Philadelphia was the fourth ranking United States city in terms of potential television audience and the largest market in which NBC did not own a television station (R. 11a, 101a, 109a).

On September 28, 1954, Broadcasting was informed that NBC desired to acquire a television station in Philadelphia. Prior to November 15, 1954, Broadcasting was informed by NBC that the latter would not renew the network affiliation agreement as to WPTZ beyond January 1, 1956. In 1955, NBC gave formal notice to Broadcasting of termination of the network affiliation agreement on January 1, 1956. Broadcasting's Philadelphia television and radio stations were sold to NBC on January 21, 1956. (R. 13a-15a, 110a-111a).

Both the Tax Court and the Court of Appeals for the Third Circuit held that the network affiliation agreement was not subject to depreciation during 1953 and 1954.

The Nature of the Decision Below

The decision below turns upon a question of law, not of fact.

There was no basic disputed question of fact to be decided either by the Tax Court or by the Court below. The contract was used in Broadcasting's business. It had

a cost basis. At the end of each of the taxable years 1953 and 1954, it had a fixed term expiring on January 1, 1956, which was subject to renewal only by mutual consent of Broadcasting and NBC. Under the FCC regulations there could be no binding agreement as of the end of the taxable years 1953 and 1954 for any renewal beyond January 1, 1956. There was no reasonable certainty of any renewal beyond January 1, 1956 and, in fact, NBC declined to renew it beyond that date. Even before the announcement in 1955 of NBC's final decision not to renew, renewal of the agreement was a matter of possibility, not of reasonable certainty. NBC informed Broadcasting in 1954 that the contract would not be renewed beyond January 1, 1956 (R. 14a, 110a).

Between January 1, 1953 and April 1, 1960, a total of 266 affiliation agreements (of which 87 were NBC affiliation agreements) were not renewed for reasons other than a station going off the air or a network acquiring its affiliate (R. 8a, 112a). The uncontradicted testimony establishes that even as a matter of business risk, no purchaser could reasonably count on more than two renewals, *i.e.*, to January 1, 1958, the terminal date used by Broadcasting for depreciation on its books and in its tax returns (R. 100a, 116a).

On those undisputed facts, the basic question in the case is one of law. What rule of law is to be applied in determining the life of such a contract for the purposes of depreciation?

Broadcasting urged the application of the rule of law applied in previous cases and rulings:

> A business contract with a fixed term is to be depreciated over the term in existence at the end of the taxable year if there is uncertainty as to renewal. It is only where it appears from the record that a renewal term or terms are reasonably certain to occur that such

renewal terms are added to the depreciable life of the contract.

The Court below repudiated that rule of law and adopted the following rule:

> A business contract with a fixed term cannot be depreciated where there is uncertainty as to the number of renewals. In order to be allowed depreciation the taxpayer must prove that there is reasonable certainty that the contract will not be renewed, either at the end of the current term or at the end of an identified future term.

While factual questions may arise in applying either rule of law, the basic question in the case is which of the rules just stated is the proper rule of law to be followed.

The rule of law adopted by the Court below resulted in a finding that the contract, although for a fixed term, had an indefinite life.

If the Court below had adopted the rule of law urged by Broadcasting, it would have found that the contract could be depreciated during 1953 and 1954 over a term ending on (1) January 1, 1956 (the term in effect at the end of the taxable years) or, at the maximum, (2) January 1, 1958 (the term over which it was depreciated on Broadcasting's books and in its tax returns).

Both the Tax Court and the Court below held that the contract was non-depreciable because Broadcasting had failed to prove with reasonable certainty the number of renewal terms which would actually occur. Under the rule of law contended for by Broadcasting, however, such proof was not required. All that Broadcasting was required to prove was that there was no reasonable certainty of renewal beyond January 1, 1956, the close of the term in effect at the end of 1953 and 1954.

REASONS FOR GRANTING THE WRIT

I

The Court below has decided an important question of Federal law in a way that is in conflict with a prior decision of that Court (*Commissioner* v. *Pittsburgh Athletic Co.*, 72 F. 2d 883 (3d Cir. 1934)) and with decisions of other Courts of Appeals (*Helvering* v. *Kansas City American Ass'n Baseball Co.*, 75 F. 2d 600 (8th Cir. 1935); *Commissioner* v. *Chicago National League Ball Club*, 74 F. 2d 1010 (7th Cir. 1935); *Bonwit Teller & Co.* v. *Commissioner*, 53 F. 2d 381 (2d Cir. 1931), *cert. denied*, 284 U. S. 690 (1932)).

(a) *Baseball Player Contracts—Helvering* v. *Kansas City American Ass'n Baseball Co.*, 75 F. 2d 600 (8th Cir. 1935); *Commissioner* v. *Chicago National League Ball Club*, 74 F. 2d 1010 (7th Cir. 1935); and *Commissioner* v. *Pittsburgh Athletic Co.*, 72 F. 2d 883 (3d Cir. 1934), all involved similar fact situations. In those cases the taxpayer ball clubs had purchased contracts with players which had one-year terms with provision for renewal for successive terms of one year each at salaries to be agreed upon between the players and the ball clubs. If an agreement as to salary was not reached, the player was to receive the same salary for the renewal term or was not to play professional baseball for one year. Many of the contracts had actually been renewed at the time of the hearing. It was held in each case that the cost of the contracts should be deducted in the year of acquisition, *i.e.*, that the renewal provisions should be disregarded, because renewals which depended on agreement of the parties were not certain. As was stated by the Court in the *Pittsburgh Athletic Co.* case (72 F. 2d at p. 884):

> ". . . the option to renew the players' contracts in the instant case might enhance the value of the contracts but would not change the period during which the contracts would become exhausted."

In the present case, the Court below denied the claimed depreciation deductions on the ground that Broadcasting had failed to prove with reasonable certainty the number of renewals of the network affiliation agreement which would actually occur. In other words, the Court below held that "uncertainty" as to renewal made the life of the affiliation agreement indefinite. That result is directly contrary to the holdings in the baseball player contract cases, as stated in the *Kansas City* case (75 F. 2d at p. 604):

> "Obviously, the options add to the value of the contracts; but it cannot be said that they extend the life of the contracts beyond one year, because of the uncertainty of their renewal."

The only distinction between those cases and the present one is that the baseball player contracts specifically provided for renegotiation of salary whereas the network affiliation agreement was silent on renegotiation of terms. That distinction is not significant. Either Broadcasting or NBC could have refused to consent to a renewal of the affiliation agreement unless any one of the terms was changed to its satisfaction. Moreover, there actually was renegotiation of the terms of the affiliation agreement with the billing rate being increased two times between June 1, 1953, and July 1, 1954. (R. 69a, 73a)

The fact that a contract is renewed by the mutual consent of the parties, with provisions which except for the term are identical to those contained in the prior contract, does not mean that there is a single contract of unlimited duration. To the contrary, a long line of decisions has held

that the renewal does not affect the deductibility of the unamortized cost, but merely extends the period over which the unamortized cost is deducted. That rule is applicable whether or not the contract itself contains a provision for renewal.*

(b) *Leases—Bonwit Teller & Co.* v. *Commissioner*, 53 F. 2d 381 (2d Cir. 1931), *cert. denied*, 284 U. S. 690 (1932), first enunciated the rule that a business contract should be depreciated over the term in effect at the end of the taxable year unless renewal provisions were reasonably certain to be exercised. That case involved a lease having a remaining term of 19 years with an option for the taxpayer to renew for an additional term of 21 years. The court held that depreciation should be based on the initial term alone because there was no evidence that the renewal option would be exercised. The taxpayer was not required to prove that the renewal option would not be exercised. It was sufficient that there was during the taxable year no reasonable certainty that it would be exercised.

The baseball contract cases simply applied the *Bonwit Teller* doctrine to business contracts other than leases. Since 1934, there has not been any case (other than the decisions in the present case) which has held that uncertainty as to the exercise of renewal provisions would prevent the depreciation of a business contract with a fixed term. As long as renewal is uncertain, the contract is to be depreciated over the term in effect at the end of the taxable year. This rule is especially applicable to television network affiliation

East Kauai Water Co., Ltd., 11 T. C. 1014 (1948); *Harris-Emery Co.*, 37 B. T. A. 958 (1938); *Cleveland Railway Company*, 36 B. T. A. 208 (1937), *acq.*, 1937-2 Cum. Bull. 5; *William Penn Hotel Co.*, 23 B. T. A. 566 (1931); *Syracuse Washing Machine Corporation*, 17 B. T. A. 11 (1929), *acq.*, IX-1 Cum. Bull. 53 (1930); *Harris Emery Co.*, 10 B. T. A. 297 (1928); *Fisher Brown*, 9 TCM 1054 (1950).

contracts, the term of which is prescribed by FCC regulation and the renewal of which must be by mutual consent of the parties.

II

The question presented in this case is of importance in the administration of Federal tax law and has not been, but should be, decided by this Court.

(a) The precise issue in this case, namely, the depreciable nature of a television network affiliation agreement, is present in at least six other cases now pending in the Tax Court and in the Court of Claims.* In addition, based upon a partial survey conducted by the National Association of Broadcasters, there appear to be at least twelve cases involving this issue now under consideration by the Internal Revenue Service. The income taxes involved in the pending cases amount to many millions of dollars. In addition, a number of cases involving the issue have not yet been considered for the Internal Revenue Service. Review by this Court would furnish the rule for decision of the many proceedings involving this issue and would prevent years of litigation.

(b) So long as the issue as to whether an affiliation agreement is depreciable for income tax purposes is in doubt, it adds an element of great uncertainty to price negotiations in the purchase and sale of television stations. A prospective purchaser can afford to pay more for an affilia-

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*_Aladdin Broadcasting Corporation_—Tax Court (No. 86155), Court of Claims (No. 458-60); _Indiana Broadcasting Corp._—Tax Court (No. 95414); _Meredith Engineering Company_—Court of Claims (No. 30-59); _Northern Pacific Television Corp._—Tax Court (Nos. 76838-41, 77411-2); _Triangle Publications, Inc._—Tax Court (Nos. 80231, 81175); _Wichita-Hutchinson Company_—Tax Court (No. 87228).

tion agreement if it is depreciable than if it is a non-depreciable asset. Until this Court settles the question, this element of uncertainty in price negotiations will continue.

(c) The decision below is also important because the rule of law which it adopts is applicable to every case involving depreciation of a contract for a term of years. Every contract can be renewed by mutual agreement whether or not there is a provision for renewal in the contract. The decision below would require every taxpayer to show that his contract will not be renewed, or just how many times it will be renewed, before it can be allowed depreciation. Such a showing is normally impossible because future intentions of private parties with respect to business contracts are not susceptible of objective proof. Thus, the decision below may have significance far beyond the field of television affiliation agreements.

III

The Court below has decided an important question of Federal law in a way that is probably in conflict with applicable decisions of this Court (*U. S.* v. *Dakota-Montana Oil Co.*, 288 U. S. 459 (1933); *Helvering* v. *R. J. Reynolds Tobacco Co.*, 306 U. S. 110 (1939)).

The *Dakota-Montana* and *Reynolds Tobacco* cases held that consistent administrative interpretation of provisions of Revenue Acts was adopted by Congress when it reenacted in succeeding Revenue Acts the provisions which had been subject to such interpretation. The depreciation provisions under which the present case arises (the Internal Revenue Codes of 1939 and 1954*) are substantially the same as

*Section 23(l) of the 1939 Code and Section 167 of the 1954 Code.

those appearing in the Revenue Act of 1918* and all succeeding Revenue Acts. The regulations with respect to the depreciation of intangibles have remained substantially the same since regulations were adopted under the Revenue Act of 1918.** The courts with the concurrence of the Commissioner of Internal Revenue have uniformly held that depreciation of business contracts over the term in effect at the close of the taxable year was required despite uncertainty as to renewal. Certain of those cases have involved contracts with renewal provisions similar to that involved in the present case. *Flynn, Harrison & Conroy, Inc.*, 21 B. T. A. 285 (1930), *acq.*, X-1 Cum. Bull. 22 (1931); *Automatic Heating and Cooling Company*, P-H 1942 B.T.A. Mem. Dec. para. 42,561 (1942); *Hickok Oil Corporation* v. *Commissioner*, 120 F. 2d 133 (6th Cir. 1941); *Kentucky Tobacco Products Co.* v. *Lucas*, 5 F. 2d 723, (D. Ky. 1925); *Powell Coal Co.*, 12 B. T. A. 492 (1928), *acq.*, VII-2 Cum. Bull. 32 (1928); *Bernicedale Coal Co.*, 16 B. T. A. 696 (1929), *acq.*, X-1 Cum. Bull. 6 (1931); *Syracuse Washing Machine Corp.*, 17 B. T. A. 14 (1929), *acq.*, IX-1 Cum. Bull. 53; *Pennsylvania Salt Manufacturing Co.*, 18 B. T. A. 1148 (1930), *acq.*, IX-2 Cum. Bull. 47 (1930); *Cleveland Railway Company*, 36 B. T. A. 208 (1937), *acq.*, 1937-2 Cum. Bull. 5; *Pasadena City Lines*, 23 T. C. 34 (1954), *acq.*, 1955-1 Cum. Bull. 6. *Cf. Van Landingham Western Sales, Inc.*, 35 B. T. A. 130 (1936).

As was stated in T. D. 4957, 1939-2 Cum. Bull. 87, with respect to leases:

> ". . . As a general rule, unless the lease has been renewed or the facts show with reasonable certainty that the lease will be renewed, the cost or other basis of the lease or the cost of improvements shall be spread only over the number of years the lease has

*Section 214(a)(8).
**Internal Revenue Regulations 45, Article 163.

to run, without taking into account any right of renewal. . . ."

The Court below has construed the re-enacted depreciation provisions and regulations in a manner inconsistent with that settled judicial and administrative interpretation.

Conclusion

For the foregoing reasons, this petition for certiorari should be granted.

Respectfully submitted,

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January 16, 1963

APPENDIX

Statutes and Regulations Involved

Internal Revenue Code of 1939, 53 Stat., Part 1, as amended, 56 Stat. 819:

Section 23. DEDUCTIONS FROM GROSS INCOME.

"In computing net income there shall be allowed as deductions:

"(1) *Depreciation.*—A reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—

"(1) of property used in the trade or business . . ."

Internal Revenue Code of 1954, 68A Stat.:

Section 167. DEPRECIATION.

"(a) *General Rule.*—There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—

"(1) of property used in the trade or business . . ."

Regulations 118:

§ 39.23 (a)-10. *Rentals.*

"(b) . . . In cases in which the lease contains an unexercised option of renewal, the matter of spreading such depreciation or amortization over the term of the original lease, together with the renewal period or periods, depends upon the facts in the particular case. As a general rule, unless the lease has been renewed or the facts show with reasonable certainty that the lease will be renewed, the cost or other basis of the lease

or the cost of improvements shall be spread only over the number of years the lease has to run, without taking into account any right of renewal."

§ 39.23 (1)-3. *Depreciation of intangible property.*

"Intangibles, the use of which in the trade or business or in the production of income is definitely limited in duration, may be the subject of a depreciation allowance. Examples are patents and copyrights, licenses, and franchises. Intangibles, the use of which in the business or trade or in the production of income is not so limited, will not usually be a proper subject of such an allowance. If, however, an intangible asset acquired through capital outlay is known from experience to be of value in the business or in the production of income for only a limited period, the length of which can be estimated from experience with reasonable certainty, such intangible asset may be the subject of a depreciation allowance, provided the facts are fully shown in the return or prior thereto to the satisfaction of the Commissioner. No deduction for depreciation, including obsolescence, is allowable in respect of good will."

Income Tax Regulations (Internal Revenue Code of 1954):

§ 1.162-11. *Rentals.*

"(b) . . .

"(2) If the lessee began improvements on leased property before July 28, 1958, or if the lessee was on such date and at all times thereafter under a binding legal obligation to make such improvements, the matter of spreading the cost of erecting buildings or making permanent improvements over the term of the original lease, together with the renewal period or periods depends upon the facts in the particular case, including the presence or absence of an obligation of renewal and the relationship between the parties. As a general rule, unless the lease has been renewed or the facts show with reasonable certainty that the lease will be renewed, the

cost or other basis of the lease, or the cost of improvements shall be spread only over the number of years the lease has to run without taking into account any right of renewal. . . ."

§ 1.167(a)-3. *Intangibles.*

"If an intangible asset is known from experience or other factors to be of use in the business or in the production of income for only a limited period, the length of which can be estimated with reasonable accuracy, such an intangible asset may be the subject of a depreciation allowance. Examples are patents and copyrights. An intangible asset, the useful life of which is not limited, is not subject to the allowance for depreciation. No allowance will be permitted merely because, in the unsupported opinion of the taxpayer, the intangible asset has a limited useful life. No deduction for depreciation is allowable with respect to goodwill. . . ."

Opinion of the Court of Appeals for the Third Circuit

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 13,839

WESTINGHOUSE BROADCASTING COMPANY, INC.

Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

Argued May 17, 1962

Before KALODNER, HASTIE and SMITH, *Circuit Judges*

OPINION OF THE COURT

(Filed October 19, 1962)

By KALODNER, *Circuit Judge*

Is a television network affiliation contract for a two-year term, automatically renewable in the absence of termination notice for successive two-year terms, a depreciable asset?

That is the question presented by this petition for review of the Decision of the Tax Court which answered it in the negative[1] premised on its determination that the con-

[1] 36 T. C. 912 (1961).

tract had "an indeterminate useful life" as of the close of the tax years here involved.

The facts critical to our disposition may be summarized as follows:

On June 1, 1953, Westinghouse Broadcasting Company, Inc. ("taxpayer") purchased from Philco Corporation ("Philco") for $8,534,000 all of the assets of television station WPTZ in Philadelphia, Pennsylvania, including its network affiliation contract with National Broadcasting Company (NBC) which was to expire on January 1, 1954.[2]

The network affiliation contract was renewable automatically for successive two-year terms unless, at least 90 days prior to the expiration of any two-year term, either party sent the other written notice of its intention not to renew[3].

[2]The network affiliation contract set forth the terms of WPTZ's affiliation with NBC. By the terms of the affiliation contract NBC agreed to supply to WPTZ a variety of network television programs, sponsored or unsponsored and to give WPTZ the right of first refusal to broadcast such programs in the Philadelphia area. WPTZ agreed, with certain exceptions, to broadcast sponsored programs of the NBC network during hours designated in the contract as "network option time". The financial arrangements set forth in the contract called for a division between WPTZ and NBC of gross billings to network advertisers for WPTZ's station time, WPTZ receiving a one-third share and NBC receiving a two-thirds share, except that for the first 24 hours of network programs broadcast by WPTZ each month billings were to be paid entirely to NBC. Billing rates were specified in the contract and were subject to change by NBC under conditions therein specified.

[3]The renewal provision reads as follows:

"23. This agreement . . . shall remain in effect for a period of two years. It shall then be renewed on the same terms and conditions for a further period of two years, and so on for successive further periods of two years each unless and until either party shall, at least three months prior to the expiration of the then current term, give the other party written notice that it does not desire to have the contract renewed for a further period."

Opinion of the Court of Appeals for the Third Circuit

The agreement between Philco and taxpayer allocated $5,000,000 of the $8,500,000 purchase price of WPTZ to the network affiliation contract, $1,500,000 to good will and the balance to tangible assets and receivables.

The network affiliation contract was automatically renewed on January 1, 1954 for a two-year term expiring January 1, 1956. On September 28, 1954 NBC informed taxpayer that it desired to acquire a television station in Philadelphia and sometime prior to November 15, 1954 taxpayer was further advised by NBC that it would not renew the network affiliation contract beyond January 1, 1956.[4] On October 1, 1955 pursuant to the 90-day notice provision of the affiliation contract NBC gave formal notice to taxpayer of termination of the network affiliation contract on January 1, 1956.

The network affiliation contract had been entered into between NBC and Philco Television Broadcasting Corporation on November 23, 1949 for a two-year term commencing January 1, 1950 and automatically renewed on January 1, 1952 for a further two-year term expiring January 1, 1954. It had been assigned to Philco by Philco Television Broadcasting Corporation on May 14, 1952 during the renewed term.

Federal Communications Commission (FCC) regulations in effect during 1953 and 1954 prohibited any contract providing for network affiliation for a term longer than two years.[5]

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[4]On May 16, 1955 taxpayer entered into an agreement with NBC whereby it agreed to exchange the assets of WPTZ and its Philadelphia radio station for the assets of NBC's Cleveland, Ohio television and radio station plus $3,000,000. The actual exchange of stations took place on January 21, 1956.

[5]47 CFR (Revised 1953) Sec. 3.658(c).

The average earnings *before taxes* of WPTZ for 1951 and 1952 were $1,704,459. The net broadcast income of WPTZ for 1951 and 1952 exceeded the broadcast income of WFIL-TV, the ABC affiliate in Philadelphia, by $748,000 and $1,250,000 respectively, and such excess was attributed by taxpayer's expert, Howard E. Stark, to WPTZ's affiliation with NBC.

Between January 1, 1953, and April 1, 1960, a total of 87 NBC affiliation agreements expired in circumstances other than a station going off the air or the acquisition of the affiliate by the network.

Taxpayer, on its books, and federal income tax returns for 1953 and 1954, depreciated its cost of the $5,000,000 network affiliation contract over a 55-month period ending January 1, 1958, i.e. the 7-month term in existence on June 1, 1953, plus two renewal terms of two years each (January 1, 1954 to January 1, 1956 and January 1, 1956 to January 1, 1958) based on taxpayer's assumption that network affiliation contracts may normally be expected to be renewed for two terms. Subsequently, in the course of the proceedings below, taxpayer contended that the network affiliation contract was depreciable over a 31-month period —the 7-month term ending January 1, 1954 and the 24-month period ending January 1, 1956 when the contract was actually terminated.

Taxpayer here contends that the Tax Court erred in its finding that the network affiliation contract did not have a "determinable useful life" as of the close of 1953 and 1954, the tax years under review. It urges that "as a matter of law, a business contract with a specific term and provision for renewal is definitely limited in duration to that term

and such renewal terms as are reasonably certain to occur," and, that "as a matter of fact, there was no reasonable certainty of renewal indefinitely with respect to the affiliation agreement" and that "the maximum period of renewal was to January 1, 1958."

The record, taken as a whole, says taxpayer, "establishes that at the time of acquisition of the affiliation agreement on June 1, 1953, two renewals, *i.e.* renewals to January 1, 1958, might be reasonably certain, but that a renewal beyond January 1, 1959, was not reasonably certain," and that "Thus the contract, under the reasonable certainty rule, had a maximum useful life of 55 months at the end of 1953 and 1954. In support, taxpayer cites the testimony of its expert, Stark: "If you could not assume two renewals, I don't think I would advise anyone to enter into a contract, but beyond that you can't foresee anything in this business."[6]

The sum of the Commissioner's position is that Section 23(1) of the Internal Revenue Code of 1939 (applicable here to the year 1953) and Section 167(a) of the Internal Revenue Code of 1954 (applicable here to 1954) provide for a depreciation deduction in circumstances where such deduction represents "a reasonable allowance for the exhaustion . . . of property used in the trade or business"; that Treasury Regulations 118 (1939) Code, Sec. 39.23(1)-3 and Treasury Regulations on Income Tax (1954 Code), Section 1.167(a)-3, provide that if an intangible asset is known from experience to be of use in the business or in the production of income for only a limited period, the length of

[6]Stark, a broker specializing in the purchase and sale of radio and television stations, played no part in the transaction in which taxpayer acquired station WPTZ from Philco.

which can be estimated with "reasonable" certainty, such intangible asset may be the subject of a depreciation allowance; that both the 1939 and 1954 Treasury Regulations impose upon the taxpayer the burden of establishing the reasonableness of the deduction for depreciation allowances;[7] and finally, that the record discloses that taxpayer had failed to establish with "reasonable" certainty that the maximum period of renewal of the network affiliation contract was to January 1, 1958.

The Tax Court held that "Insufficient evidence was introduced from which could be calculated either the average useful life of network affiliation contracts or their useful life span", and further stated its conclusion "that petitioner [taxpayer] has not only failed to persuade us that the contract had a 55-month useful life but also that it has failed to persuade us respondent [Commissioner] erred in his determination that the contract had an indeterminable useful life".

On review of the record we agree with the Tax Court's holding that taxpayer failed to prove that at the close of the taxable years 1953 and 1954 it was "reasonably certain" that the network affiliation contract had a maximum useful life but 55 months from the date of its acquisition by taxpayer on June 1, 1953.

The burden of proof to do so was on taxpayer not only under the applicable revenue statutes and the Treasury Regulations pertaining to them, earlier cited, but by reason of the well-settled principle that the Commissioner's determination of a deficiency in tax bears a presumption of cor-

[7]Treas. Reg. 118, Sec. 39.23(*l*)-5 (1939); Treas. Reg. on Income Tax Sec. 1.167(b)-O (1954 Code).

rectness. Hoffman v. Commissioner, 298 F. 2d 784, 788 (3 Cir. 1962).

Taxpayer did not adduce any testimony to the effect that based on "experience" in the television industry the number of renewals of the network affiliation contract could be "estimated" with "reasonable certainty" or "reasonable accuracy" as required by the Treasury Regulations earlier cited.

While taxpayer's expert, Stark, in substantiating the $5,000,000 consideration paid for the network affiliation contract, testified that he had assumed a useful life for the contract which contemplated two renewals after acquisition, or 55 months in this case, he did not say that his assumed premise of such two renewals was based on "experience" with such contracts. All that Stark said was that it was the "practice" of experts in evaluating network affiliation contracts "to anticipate the likelihood of two separate renewals . . . following the expiration of the unexpired term of the contract," to which he added that in his post-evaluation of the contract here involved he had in mind that anticipation and "the hope that it would be continued beyond that date [two separate renewals]."

It must be stressed that nowhere in his testimony did Stark say that the "practice" of experts in anticipating two renewals of network affiliation contracts was based on "experience" with respect to contract renewals.

Under the circumstances we agree with the Tax Court that the "practice" of the experts in figuring on two renewals of a network affiliation contract was not "a sufficient indication of that contract's probable useful life."

Nor can any probative value with respect to the "probable useful life" of the network affiliation contract here be

attributed to the stipulated fact that "between January 1, 1953 and April 1, 1960, a total of 87 NBC affiliation agreements expired in circumstances other than a station going off the air or the acquisition of the affiliate by the network" since there was no evidence as to the actual life span of those agreements or as to the number of their renewals.

This too must be said. Taxpayer based its 55-month useful life estimate of the network affiliation contract on its premise that there was reasonable certainty of only 48 months plus the 7 months of its unexpired term. The premise was in turn sub-based, so to say, on the theory that network affiliation contracts have a life span of 72 months, their original two-year term and two renewals. Taxpayer disregards the fact that the network affiliation contract here had actually run for 24 months (January 1, 1950 to January 1, 1952) prior to the renewed term (January 1, 1952 to January 1, 1954) during which it was acquired by taxpayer on June 1, 1953.

It would serve no useful purpose to discuss the cases cited by taxpayer and the Commissioner since the facts in those cases vary significantly from those existing here.

For the reasons stated the decision of the Tax Court will be affirmed.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.